



CONGRESSIONAL BUDGET OFFICE COST ESTIMATE

December 5, 1997

H.R. 10 **Financial Services Competition Act of 1997**

As reported by the House Committee on Commerce on November 3, 1997

SUMMARY

H.R. 10 would abolish the federal thrift charter, thus allowing the merger of the bank and thrift insurance funds, and would eliminate certain barriers to ties between insured depository institutions and other financial and commercial firms. While these changes could affect the government's spending for deposit insurance, CBO has no basis for predicting whether the long-run costs of deposit insurance would be higher or lower than under current law. Because insured depository institutions pay premiums to cover these costs, any such changes would have little or no impact on the budget over time. CBO estimates that implementing the bill would increase other direct spending by \$4 million in 1998 and \$103 million over the 1998-2002 period, and would decrease revenues by less than \$500,000 in 1998 and \$16 million over the 1998-2002 period. Assuming appropriation of the necessary amounts, CBO estimates that several agencies would spend between \$1 million and \$2 million annually to carry out the provisions of the bill, once fully implemented. Because H.R. 10 would affect direct spending and receipts, pay-as-you-go procedures would apply.

H.R. 10 contains several intergovernmental mandates as defined in the Unfunded Mandates Reform Act (UMRA), but CBO estimates that the costs of complying with these mandates would total less than \$10 million annually and thus would not exceed the threshold established under that act (\$50 million in 1996, adjusted annually for inflation). H.R. 10 also would impose new private-sector mandates as defined in UMRA, but we estimate that the costs of complying with those mandates would not exceed the threshold set in UMRA (\$100 million in 1996, also adjusted annually for inflation) in any one year for the first five years that mandates are effective.

DESCRIPTION OF THE BILL'S MAJOR PROVISIONS

H.R. 10 would:

- require all federally chartered savings associations to convert to a national bank or state charter within two years after date of enactment, merge the Office of Thrift Supervision (OTS) with the Office of the Comptroller of the Currency (OCC), and allow the merger of the Savings Association Insurance Fund (SAIF) and the Bank Insurance Fund (BIF);
- permit affiliations of banking, securities, and insurance companies;
- with certain revenue limitations, allow financial holding companies to affiliate with commercial firms;
- provide for a new type of wholesale financial institution (WFI) that does not accept retail insured deposits and would be subject to the Community Reinvestment Act of 1977;
- create a new system for regulating and supervising financial holding companies, and clarify the functional authority of various federal and state regulators of financial institutions;
- establish a nonprofit corporation, the National Association of Registered Agents and Brokers, to provide uniform licensing and training standards for insurance agents;
- establish an expedited legal process for resolving disputes as to whether or not a product qualifies as insurance, and whether or not a state law regulating an insurance activity is preempted by federal law;
- require the General Accounting Office (GAO) to analyze the costs and benefits of creating a government seal for identifying products not insured by the BIF or the SAIF;
- amend the Securities Exchange Act of 1934 to define bank employees or bank affiliates as “brokers” if they conduct certain activities; and
- shift from the financial regulatory agencies to the Department of Justice (DOJ) the authority to review the competitive effects of the antitrust laws involving mergers of depository institutions.

ESTIMATED COST TO THE FEDERAL GOVERNMENT

H.R. 10 would make a number of changes affecting direct spending and revenues, which would result in increased spending by the banking regulatory agencies and a decrease in the annual payment—recorded as revenues—that the Federal Reserve remits to the Treasury. CBO estimates that direct spending would increase by about \$103 million over the 1998-2002 period. We estimate that enacting H.R. 10 would decrease revenues by \$16 million over the same period. The bill also would increase discretionary spending by an estimated \$6 million over the 1998-2002 period, assuming appropriation of the necessary amounts. The estimated budgetary impact of H.R. 10 is shown in the following table. The budgetary effect of this legislation on outlays falls within budget function 370 (commerce and housing credit). The legislation would also affect revenues (governmental receipts).

	By Fiscal Year, in Millions of Dollars				
	1998	1999	2000	2001	2002
DIRECT SPENDING					
Spending Under Current Law ^a					
Estimated Budget Authority	0	0	0	0	0
Estimated Outlays	-4,261	-2,853	-1,167	-482	-290
Proposed Changes					
Estimated Budget Authority	0	0	0	0	0
Estimated Outlays	4	29	27	21	22
Spending Under H.R. 10 ^a					
Estimated Budget Authority	0	0	0	0	0
Estimated Outlays	-4,257	-2,824	-1,140	-461	-268
CHANGES IN REVENUES					
Estimated Revenues ^b	c	-4	-4	-4	-4
CHANGES IN SPENDING SUBJECT TO APPROPRIATION					
Estimated Authorization Level	1	2	1	1	1
Estimated Outlays	1	2	1	1	1

a. Includes spending for all deposit insurance activities (subfunction 373).

b. Includes changes in the Federal Reserve surplus. A negative sign indicates a decrease in revenues.

c. Reduction in revenues of less than \$500,000.

BASIS OF ESTIMATE

Direct Spending and Revenues

H.R. 10 could affect direct spending for deposit insurance by increasing or decreasing amounts paid by the insurance funds to resolve insolvent institutions and to cover the administrative expenses necessary to implement its provisions. Changes in spending related to failed banks and thrifts could be volatile and vary in size from year to year, but any such costs would be offset by insurance premiums, and thus their budgetary impact would be negligible over time. The bank regulators would also incur expenses related to the proposed legislation, but not all of these costs would be offset by fees. Finally, H.R. 10 would affect revenues by reducing annual payments from the Federal Reserve to the Treasury.

Deposit Insurance Funds. Enacting H.R. 10 could affect the federal budget by causing changes in the government's spending for deposit insurance, but CBO has no clear basis for predicting the direction or the amount of such changes. Changes in spending for deposit insurance could be significant in some years, but would have little or no net impact on the budget over time.

Title IV would convert to national banks all federal savings institutions in existence within two years of the date of enactment, thus allowing the merger of the BIF and the SAIF. Both funds hold reserves in excess of the levels mandated by statute, and thus the combined fund would be well-capitalized initially. The SAIF insures far fewer and more geographically concentrated institutions than does the BIF, and those institutions focus on housing finance. A combined insurance fund thus could benefit from diversifying geographic and product risks that could lower the probability that the fund would become insolvent.

Other provisions in the bill could affect spending by the deposit insurance funds. Some are likely to reduce the risks of future bank failures. For example, H.R. 10 would permit affiliations of banking, securities, and insurance companies, thereby giving such institutions the opportunity to diversify and to compete more effectively with other financial businesses. Changes in the marketplace, particularly the effects of technology, have already helped to blur the distinctions among financial service firms. Further, regulatory and judicial rulings continue to erode many of the barriers separating different segments of the financial services industry. For example, banks now sell mutual funds and insurance to their customers and, under limited circumstances, may underwrite securities. At the same time, some securities firms offer checking-like accounts linked to mutual funds and extend credit directly to businesses. Because H.R. 10 would streamline the regulatory and legal structure that currently governs bank activities, CBO expects that its enactment would allow banks to compete more effectively in the rapidly evolving financial services industry. Diversifying

income sources also could result in lower overall risks for banks, assuming that the expansion of their activities is accompanied by adequate safeguards. The bill would create “firewalls” to protect the banking components of a financial services organization from its riskier securities, insurance, or other financial activities, and would prohibit or limit certain transactions between banks and affiliates, hopefully preventing financial and informational abuses and conflicts of interest.

H.R. 10 also would allow banks to expand into relatively unfamiliar activities, thus possibly increasing the risk of bank failures. The bill would allow financial holding companies to engage in certain specified financial activities, as well as some activities that are not financial in nature. Financial holding companies could own commercial firms as long as the consolidated annual revenues would not exceed 5 percent of the holding company's gross revenues or \$500 million, whichever is less.

Permitting insured banks to diversify into product areas where they have little experience raises questions about the adequacy of the regulators’ ability to protect the insured entities and the insurance funds. Several federal banking regulators have expressed uncertainty about their ability to maintain adequate safeguards between the transactions of the insured institutions and their commercial affiliates and subsidiaries, although their concern has typically focused on levels exceeding the 5 percent threshold. A major consideration would be preventing nonbanking losses in affiliates from draining the resources of the insured banks. To maintain safety and soundness in the banking system, H.R. 10 would require a holding company to develop procedures for identifying and managing risk. Nonetheless, experience with mixing commerce and banking in the United States has been limited. Ultimately, strong supervision and monitoring by regulators, which history has demonstrated is critical in limiting the exposure of the taxpayers during times of financial stress, would be essential to avoid additional losses to the deposit insurance fund.

If losses to the deposit insurance fund were to increase as a result of enacting H.R. 10, the BIF would increase premiums that banks pay for deposit insurance. Similarly, if losses were to decrease, banks might pay smaller premiums in the future. As a result, the net budgetary impact is likely to be negligible over time in either case.

Conversion of Thrift Institutions. Two years after the date of enactment, all existing federal thrifts would be converted to national banks, and all state-chartered thrifts would be treated as state-chartered banks. At the same time, the OCC and the OTS would be merged, along with the bank and thrift deposit insurance funds, the BIF and the SAIF. Thrifts would no longer be required to maintain membership in the Federal Home Loan Bank (FHLB) system. Finally, unitary thrift holding companies now in existence would retain all their current powers after conversion to a bank charter.

Merging the OTS and the OCC should result in long-term savings to the financial institutions that pay annual fees to cover the administrative expenses of the agencies. CBO estimates that reducing overhead and streamlining the examination process would result in cost savings of between \$10 million and \$15 million annually, once the merger is completed. The net budgetary effect of any such savings would be zero over time, however, because any reduction in expenses would result in a corresponding decrease in fee income.

Initially, CBO anticipates that the transition costs to move employees, to cover cancellations of leases, to train employees, to pay the costs of reductions-in-force, and to reprogram payroll, accounting, and other data systems, would cost about \$15 million over the 1999-2000 period. Based on information from the OTS and the OCC, we expect that the OTS would tap its existing reserve funds to pay these transition costs. Given the current OTS surplus, the agencies do not anticipate that fees paid by banks and the newly converted thrifts would be increased to replenish any reserves used for this purpose. As a result, CBO estimates that outlays would increase by \$8 million in 1999 and by \$7 million in 2000.

H.R. 10 would require about 1,100 federal thrifts to choose a new charter—either a state depository charter or a national bank charter. If no action is taken, the institution would automatically be designated a national bank. Under current law, the OCC is responsible for regulating national banks; the Federal Deposit Insurance Corporation (FDIC) regulates state-chartered banks that are not members of the Federal Reserve System; and the Federal Reserve regulates state-chartered member banks and bank holding companies. CBO expects that most thrifts would retain their state or federal affiliation, and that most large thrifts would become national banks, thus coming under the OCC's authority. The FDIC would supervise some smaller thrifts that shift their federal charters to either state thrift or state bank charters, as well as holding companies where the lead bank is state-chartered and not a member of the Federal Reserve System. We expect that abolishing the federal thrift charter would have a minimal effect on the supervisory activities of the Federal Reserve System. In addition, all the federal regulators are likely to have some additional examination activity associated with banks and nonfinancial affiliates.

As previously noted, with the exception of transition costs, transferring supervisory responsibility for newly chartered national banks from the OTS to the OCC would have no net budgetary effect, because both agencies charge fees to cover all their administrative costs. That is not the case with the FDIC, however, which uses deposit insurance premiums paid by all banks to cover the expenses it incurs to supervise state-chartered banks. Because the BIF and the SAIF are well-capitalized, most banks and thrifts pay no premiums for deposit insurance at this time. Further, any increase in administrative costs triggered by H.R. 10 is not likely to result in future rate increases. CBO estimates that the FDIC would spend an additional \$2 million in 1998 and about \$18 million annually beginning in 1999 on regulatory

and examination costs associated with its role in maintaining the safety and soundness of the institutions it supervises. CBO expects no significant administrative savings or costs from merging the BIF and the SAIF into a combined fund.

Other Bank Regulatory Costs. The Federal Reserve, the Securities and Exchange Commission (SEC), and state and federal banking regulators—the OCC, the FDIC, and the OTS—would have primary responsibility for monitoring compliance with the statute. H.R. 10 would impose consumer protection regulations governing retail sales of nondeposit products and other requirements. The regulatory agencies would be required to develop programs for promoting housing finance, and to implement new regulations, policies, and training procedures related to securities, insurance, and other areas. CBO expects that spending by the FDIC would total about \$1 million in 1998 and \$2 million annually for these new activities and for costs associated with monitoring compliance with the Community Reinvestment Act by the newly converted thrifts. The OCC and the OTS would also incur expenses for these purposes, but they would be offset by increased fees, resulting in no net change in outlays for those agencies.

Revenues. Based on information from the Federal Reserve, we estimate that H.R. 10 would require the Federal Reserve to incur added examination costs of about \$4 million per year once the bill's requirements are fully effective in 1999. These costs would be necessary to supervise the activities of the new financial holding companies, as well as the new WFIs, which would not accept retail insured deposits. The Federal Reserve's cost of processing applications could also be affected. Applications for nonbanking activities could decrease but applications for the newly authorized activities of holding companies could increase. We expect that these changes would be roughly offsetting, resulting in no net budgetary impact. In addition, small savings would result from the bill's general requirement that the Federal Reserve not examine certain affiliates for whom the primary regulatory and supervisory responsibility lies with other federal entities. The estimated savings would total less than \$500,000 per year.

Because the Federal Reserve system remits its surplus to the Treasury, changes in its operating costs would affect governmental receipts. The net effect of the changes in this bill would be to reduce governmental receipts by an estimated \$16 million over the 1998-2002 period.

Spending Subject to Appropriation

A number of federal agencies would be responsible for monitoring changes resulting from enactment of H.R. 10. CBO estimates that total costs, assuming appropriation of the

necessary amounts, would be about \$1 million each year once the provisions of the bill are fully implemented, primarily for expenses of the SEC. The SEC would incur costs to monitor market conditions, to examine firms, and to investigate practices to ensure compliance with the statute. We expect these additional rulemaking, inspection, and administrative expenses of the SEC would total about \$1 million annually.

H.R. 10 would require GAO to conduct a study of various methods of informing consumers about products that the FDIC does not insure. CBO estimates that GAO would spend less than \$1 million through 1999 to collect and analyze data and prepare the report. Finally, DOJ would assume primary responsibility for streamlining the review of the antitrust implications of bank acquisitions and mergers. Based on information from DOJ, we expect that the department would continue to work with federal banking regulators to monitor such activity, and would incur no significant additional cost as a result of this change.

PAY-AS-YOU-GO CONSIDERATIONS

Section 252 of the Balanced Budget and Emergency Deficit Control Act of 1985 sets up pay-as-you-go procedures for legislation affecting direct spending or receipts. Legislation providing funding necessary to meet the deposit insurance commitment is excluded from these procedures. CBO believes that the various costs of H.R. 10 related to consumer protection and housing lending do not meet the exemption for the full funding of the deposit insurance commitment and thus would have pay-as-you-go implications. We estimate that direct spending changes resulting from the increase in the FDIC's supervisory costs associated with activities other than those related to safety and soundness would total about \$1 million in 1998 and \$2 million annually beginning in 1999. Costs for similar activities of the OCC and the OTS would be offset by increases in fees of an equal amount, resulting in no significant net budgetary impact for those agencies.

CBO expects that the Federal Reserve would incur additional expenses associated with consumer and housing issues that are not directly related to protecting the deposit insurance commitment. We estimate that the resulting increase in regulatory and other costs would reduce the surplus payment that the Federal Reserve remits to the Treasury by less than \$500,000 annually.

The net changes in outlays and governmental receipts that are subject to pay-as-you-go procedures are shown in the following table. For the purposes of enforcing pay-as-you-go procedures, only the effects in the budget year and the succeeding four years are counted.

	By Fiscal Year, in Millions of Dollars									
	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007
Changes in outlays	1	2	2	2	2	2	2	2	2	2
Changes in receipts	0	0	0	0	0	0	0	0	0	0

ESTIMATED IMPACT ON STATE, LOCAL, AND TRIBAL GOVERNMENTS

H.R. 10 contains several intergovernmental mandates as defined in UMRA. CBO estimates that the total cost of complying with these mandates—primarily preemptions of state laws—would be less than \$10 million a year. The bill contains other provisions, which are not mandates, but which CBO estimates would affect the budgets of state and local governments. H.R. 10 would not impose mandates or have other budgetary impacts on tribal governments.

Mandates

A number of provisions in H.R. 10 would preempt state banking, insurance, and securities laws. For example, states would not be allowed to prevent banks from engaging in certain activities (such as selling insurance and securities) authorized under the act, nor would they be allowed to restrict the reorganization of mutual insurers. Such preemptions are mandates under UMRA. Based on information provided by the National Association of Insurance Commissioners (NAIC), the Conference of State Bank Supervisors (CSBS), and the North American Securities Administrators Association (NASAA), CBO estimates that enactment of these provisions would not result in direct costs or lost revenue to state governments because, while they would be prevented from enforcing certain rules and regulations, they would not be required to undertake any new activities.

Title III of the bill would require a majority of states (within three years of enactment of H.R. 10) to enact uniform laws and regulations governing the licensing of individuals and entities authorized to sell insurance within the state. If a majority of states do not enact such laws, certain state insurance laws would be preempted and a National Association of Registered Agents and Brokers (NARAB) would be established. The purpose of the association would be to provide a mechanism through which uniform licensing, continuing education, and other qualifications could be adopted on a multistate basis. Membership in NARAB would be voluntary and open to any state-licensed insurance agent.

If NARAB is established, states would maintain the core functions of regulating insurance, such as licensing, supervising, and disciplining insurance agents and protecting purchasers of insurance from unfair trade practices, but certain state laws would be preempted. Specifically, Title IV would prevent states from discriminating against members of NARAB by charging different licensing fees based on residency. Based on information from the NAIC about the number of out-of-state agents and current state license fees, CBO estimates that these preemptions would result in the loss of license fees to states totaling less than \$10 million a year.

Other Impacts

Enactment of H.R. 10 would result in additional costs and revenues to state regulatory agencies. Certain provisions of the bill could lead to the establishment of new bank subsidiaries involved in insurance or securities activities. Because most states already allow banks to be involved in such activities, we expect that any additional costs would be small. In general, costs incurred by states would be offset by additional examination and licensing fees.

Title IV also could result in additional work for state banking agencies if federal thrifts whose charters are being abolished under the bill choose to become state-chartered financial institutions. Based on information from the CSBS, CBO estimates that any such increase in workload would be modest and that any costs would be offset by an increase in receipts from bank examination fees.

Finally, certain provisions in Title II, which would expand the definitions of "investment adviser," "broker," and "dealer," would increase the number of individuals and organizations registering with states, thereby increasing fee revenues. Based on information from NASAA, CBO estimates that income from additional filing and registration fees would not be significant.

ESTIMATED IMPACT ON THE PRIVATE SECTOR

H.R. 10 would impose several new private-sector mandates as defined by the Unfunded Mandates Reform Act of 1995. The mandates in the bill would affect federal savings associations, banking firms, and other organizations that engage in financial activities. CBO estimates that the net direct costs of those mandates would probably not exceed the statutory threshold for private-sector mandates (\$100 million in 1996 dollars, adjusted annually for inflation) in any one year for the first five years that the mandates are effective.

The bill contains several new mandates on businesses in the financial services sector. If enacted, major provisions in H.R. 10 would:

- force all federally chartered thrifts to convert to another charter within two years after enactment;
- require banking organizations to adopt several consumer protection measures affecting sales of insurance products;
- limit the authority of federally-chartered banks (national banks) that currently sell title insurance, and end the authority to sell title insurance for national banks that do not now sell such insurance;
- end the blanket exemption under the Securities Exchange Act of 1934 for brokers and dealers that conduct business in banks, making them subject to regulation by the Securities and Exchange Commission; and
- end the exemption under the Investment Advisers Act of 1940 for bank investment advisers, making them subject to SEC examination and registration requirements.

CBO estimates that, by the second year after enactment, federally chartered thrifts would incur a one-time cost of about \$14 million for converting to another charter. In addition, banking organizations would incur additional costs to comply with new mandates in the bill. Greater uncertainty exists about the additional costs to banks because many of the mandates on banks are highly dependent on the actions of regulators. CBO cannot estimate the costs to comply with future regulations on securities activities in banks, but the costs to banks of other mandates in the bill are not likely to be substantial. The direct costs of mandates on banks would be at least partially offset by savings from changes the bill would make to expand the powers of banking organizations.

Elimination of the Federal Thrift Charter

Two years after enactment, Title IV of the bill would require federal savings associations to be converted, by operation of law, to national banks. The bill would grandfather all current thrift powers except for those of thrift holding companies not in existence or not on record as having filed to become a holding company by September 16, 1997. The direct costs of conversion could include such items as conversion fees to a new chartering agency, the costs of replacing signs and stationery, the cost of a pre-conversion examination, and legal costs associated with adopting and conforming with the new charter. CBO assumes that the

chartering agency would not charge federal savings associations a conversion fee and that the converting federal savings associations would not incur the legal costs associated with filing for conversion or the costs of a pre-conversion examination. Therefore, the direct costs of converting to a national bank would be the costs of replacing signs and stationery. Given that federal thrifts would have two years for this transition, new stationery would not necessarily be an additional cost. The cost to replace signs, assuming a cost of about \$2000 per branch, would amount to about \$14 million.

Consumer Protection Regulations—Insurance Sales

Section 308 would direct the federal banking regulators to issue, within one year of enactment, final consumer protection regulations that would govern the sale of insurance by any bank or by any person at or on behalf of a bank. According to the bill, the regulations should include requirements for: (1) anti-coercion rules (prohibiting banks from misleading consumers into believing that an extension of credit is conditional upon the purchase of insurance); (2) easily understandable disclosures as to whether a product is insured by the FDIC; (3) an appropriate delineation of the settings and circumstances under which insurance sales should be physically segregated from bank loan and teller activities; (4) standards limiting compensation systems for insurance referrals by bank tellers or loan personnel; (5) proper licensing and qualification of bank insurance personnel; and (6) prohibitions on insurance discrimination against victims of domestic violence.

Except for the anti-coercion and anti-discrimination provisions, the provisions in section 308 are based on current industry guidelines issued in 1994 by bank regulators in an Interagency Statement on Retail Sales of Non-deposit Investment Products. The anti-coercion provision is similar to the anti-tying provision in current law. The bill would direct the federal banking agencies to jointly establish regulations to prohibit consideration of domestic abuse as a criterion in any decision on insurance underwriting, pricing, renewal of insurance policies, or payment of insurance claims for any insurance activity conducted by or at a bank or by a bank representative. Many industry experts indicate that such a rule would not impose significant costs on the industry. Other new regulations would largely codify a modified version of existing guidelines drafted by the federal banking regulators and, therefore, would not likely impose large incremental costs on banks that currently engage in insurance activities.

Regulation of Other Insurance Activities

Several provisions in the bill would change how current insurance activities and future insurance products are regulated. H.R. 10 would require that all insurance activity be "functionally regulated." Because the bill would grandfather most existing insurance activities, the incremental costs of these mandates would be small.

Section 304 of the bill would continue a ban on insurance underwriting by national banks and their subsidiaries, except for products they are currently underwriting and were allowed to underwrite as of January 1, 1997. These exceptions do not include annuities and title insurance, which banks would not be allowed to underwrite. Section 306 would generally prohibit a national bank and its subsidiaries from selling or underwriting title insurance, but would grandfather those activities that a bank (or its subsidiaries) was actively and lawfully engaged in before the date of enactment. However, if a national bank had an insurance underwriting affiliate or subsidiary, any title insurance underwriting or sales activities would have to be conducted by such affiliate or subsidiary. Section 306 would also grant national banks and their subsidiaries the authority to sell title insurance in a state that allowed state-chartered banks to sell title insurance as of January 1, 1997.

Regulation of Securities Activities and Investment Adviser Services

H.R. 10 would end the current blanket exemption for banks from being treated as brokers or dealers under the Securities Exchange Act of 1934. Securities activities of banks would, therefore, be subject to SEC regulation, with some exceptions. The bill would exempt from SEC regulation the securities activities of banks handling fewer than 500 transactions annually. Many of the roughly 300 small banks that currently provide brokerage services on bank premises would fall under this exemption. Sections 201 and 202 would exempt several traditional securities activities of banks from the registration requirements and regulations that apply to brokers or dealers under SEC regulation. The exemptions would cover many products and services that banks currently offer as agents so that they would not trigger SEC regulation. However, certain bank products and services related to securities—self-directed IRAs and private placements, for example—may not be exempt under H.R. 10. If regulators determine that any of those products would no longer be exempt under the bill, banks would either have to become registered brokers or dealers or they would have to channel the non-exempt activities through an affiliated broker-dealer. A substantial number of banks that currently handle securities activities have a broker-dealer affiliate so that the incremental cost of complying with SEC regulation would involve moving non-exempt activities to such an affiliate. Because of uncertainty with regard to how regulators would determine which

products would be exempt, CBO cannot estimate the incremental costs of compliance for banks currently engaging in activities that would be affected.

Section 205 would require bank regulatory agencies to establish record-keeping requirements for banks that claim the exemptions allowed under sections 201 and 202. The impact of the new reporting requirements on banks that would be allowed an exemption is uncertain because it would depend on future federal rulemaking. The bill directs regulators to make the new requirements sufficient to demonstrate compliance with the terms of the exemption. Because CBO has no basis for predicting how this provision would be implemented, we cannot estimate the costs of new requirements on banks. However, given the infrastructure in place that supports current reporting requirements, we expect that the incremental costs of the new requirements would be small.

Section 217 would amend the Investment Advisers Act to subject banks that advise mutual funds to the same regulatory scheme as other advisers to mutual funds. Currently, about 120 large bank holding companies engage in investment adviser activities. Before enactment of the National Securities Markets Improvement Act of 1996, the SEC charged a fee of \$150 to register investment advisers. Because of the 1996 act, the SEC is in the process of formulating a fee that will be based on the expected cost of administering the registration program, and the expected number of registrants. Banking organizations that continue to be investment advisers would have to pay this new registration fee annually and maintain books and records according to SEC rules. Inasmuch as the SEC is still in the very early stages of designing a system for registration, CBO has no basis for estimating the incremental costs of registering with the SEC. These costs, however, are not expected to be large.

Section 214 would amend the Investment Company Act to require any person issuing or selling the securities of a registered investment company that is advised or sold through a bank to disclose that an investment in the fund is not insured by the Federal Deposit Insurance Corporation or any other government agency. Typically, the costs of creating a standard disclosure form and distributing such a statement at the time of a transaction are not large.

PREVIOUS CBO ESTIMATE

On September 12, 1997, CBO prepared a cost estimate for H.R. 10, as reported by the House Committee on Banking and Financial Services on July 3, 1997. That version of the bill includes provisions that would change the financial responsibilities of the Federal Home Loan Bank (FHLB) System by replacing the \$300 million annual payment made by the FHLBs for interest on bonds issued by the Resolution Funding Corporation with an

assessment set at 20.75 percent of the FHLBs' net income. As a result, CBO estimated that FHLB payments would increase by \$109 million and Treasury outlays would decrease by an equal amount over the 1998-2007 period. The version of H.R. 10 reported by the Committee on Commerce does not change the amount of the FHLB payments. Therefore, the bill no longer would impose a private-sector mandate on the FHLB System and thus, the aggregate direct cost of private-sector mandates in this version of the bill would fall below the statutory threshold.

The Banking Committee's version of H.R. 10 also would create a National Council on Financial Services to define products that are financial in nature, identify the appropriate regulator, and regulate disputes involving those definitions. CBO estimated that the council would incur costs of \$2 million to \$3 million annually. The Commerce Committee's version would not create such a council. The costs of other provisions related to regulatory and supervisory responsibilities of the federal financial regulators do not differ significantly.

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